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Conflict of Laws—Secured Transactions—UCC.—Casterline v. General Motors Acceptance Corp.

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so dictates.[24] Furthermore, mere suspicions of improper actions, without more, are not enough to require the imposition of Chapter X.[25]

In the principal case, the court held that proceedings under Chapter XI are not available to a debtor corporation with publicly held securities when there is a need for a thorough reorganization of the corporation's capital structure.[26] Here, a composition of creditors, without more, would have presented a substantial question of fairness to the debenture holders and, at the same time, the financial history and condition of the debtor indicated that the interests of the investing public, and those of the SEC, could not be adequately represented under the Chapter XI proceedings.

It would appear then, that Chapter XI is available to large publicly held corporations only when the debtor's plan proposes no more than a simple composition of unsecured debts, when there is no reason to believe that management has acted in bad faith or that it is incompetent, and when priority rights of creditors are not jeopardized.

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Conflict of Laws—Secured Transactions—UCC.—***Casterline v. General Motors Acceptance Corp.***[1]—On October 14, 1957, a New York dealer sold by conditional sale an automobile to Simon and the same day assigned the contract to appellant General Motors Acceptance Corporation. Within two days the automobile passed through a succession of purchasers and lastly was sold to a Pennsylvania purchaser for value in Wilkes-Barre.[2] The original vendor filed his conditional sales contract in the registry of Bronx County, New York, on October 21. No payments on the contract having been made by December, the appellant repossessed the vehicle. From an adverse decision in his action of replevin, the plaintiff appealed to the Superior Court of Pennsylvania. HELD: The vendor's interest is prior to that of the purchaser.

The problem is the interplay of the provisions of the Uniform Conditional Sales Act with those of the Uniform Commercial Code as applied by Pennsylvania. New York law, which governs the original sale, provides that the seller's rights reserved by conditional sale are void as to any bona fide purchaser for value without notice unless the contract or copy is filed in the appropriate filing district within ten days after the sale.[3] New York does not have a title certificate law. In contrast, the Pennsylvania conditional vendor must note his encumbrance on the certificate of title to "perfect" his interest under the Code Section 9-302(3)(b) in conjunction with the Pennsylvania Motor Vehicle Code.[4]

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[24] SEC v. Wilcox-Gay Corp., supra note 23.

[25] 6 Collier, Bankruptcy ¶ 0.11 (1940), In re Transvision, supra note 22.

[26] Supra note 1, at 791.

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[1] 171 A.2d 813 (Pa. Super. Ct. 1961).

[2] The ultimate purchaser was refunded the purchase price by his seller, the plaintiff Casterline, and was not involved in the litigation. The court attached no significance to the fact that Casterline was a dealer.

[3] N.Y. Pers. Prop. Law § 65.

[4] Pa. Stat. Ann. tit. 12A § 9-302(3)(bb), and tit. 75 §§ 31-42.

The conflict of laws rules of the Code provide that a security interest which has attached to personal property according to the law of the situs, before its removal into the state, will be considered perfected in Pennsylvania for four months after entry if the interest was already perfected in the jurisdiction wherein the interest had attached.[5] The court decided that the New York filing statute was *pari materia* with the Code's perfection prerequisite, hence compliance with New York law should afford the New York vendor the same protection in this case as is given the Pennsylvania holder of an interest perfected under the Code. It further decided that a New York security interest is perfected at once when the contract is made subject to losing its priority if the contract is not filed in time.

Most courts recognize that a security interest in a chattel, properly attached and duly recorded according to the law of the state wherein the interest was created and the chattel then located, will, if valid in such state, be valid against subsequent purchasers and creditors in the state to which the property is removed, if such removal is without the knowledge or consent of the interest holder.[6] Just as the owner of stolen property can follow the

[5] Pa. Stat. Ann. tit. 12A § 9-103(3). The present version presents an interesting improvement in the wording of the Code. The 1958 Official Text provides in § 9-103:

> (3) If personal property other than that governed by subsections (1) and (2) is already subject to a security interest when it is brought into this state, the validity of the security interest in this state is to be determined by the law (including the conflict of laws rules) of the jurisdiction where the property was when the security interest attached. However, if the parties to the transaction understood at the time that the security interest attached that the property would be kept in this state and it was brought into this state within 30 days after the security interest attached for purposes other than transportation through this state, then the validity of the security interest is to be determined by the law of this state. If the security interest was already perfected under the law of the jurisdiction where the property was when the security interest attached and before being brought into this state, the security interest continues perfected in this state for four months and also thereafter if within the four month period it is perfected in this state. The security interest may also be perfected in this state after the expiration of the four month period; in such case perfection dates from the time of perfection in this state. If the security interest was not perfected under the law of the jurisdiction where the property was when the security interest attached and before being brought into this state, it may be perfected in this state; in such case perfection dates from the time of perfection in this state.

The earlier draft, enacted by Pennsylvania and applicable in the principal case, provided:

> (3) . . . If the security interest was already perfected under the law of the jurisdiction where the property was kept before being brought into the state, the security interest continues perfected here for four months and also thereafter if within the four month period it is perfected here. . . . If the security interest was not perfected under the law of the jurisdiction where the property was kept before being brought into the state, it may be perfected here; in such case perfection dates from the time of perfection in this state.

By amendment of October 2, 1959, P.L. 1023, § 9, Pennsylvania adopted the improved draft.

[6] Ragner v. General Motors Acceptance Corp., 66 Ariz. 157, 185 P.2d 525 (1947); Chetopa State Bank v. Manes, 221 Ark. 784, 255 S.W.2d 957 (1953); Atlia v. Bocklus, 39 Cal.2d 635, 248 P.2d 745 (1952); Morris Plan Bank v. Terrell, 4 Del. (5 Terry) 533, 62 A.2d 452 (1948); Continental National Bank v. Short, 101 Ga. App. 304, 113 S.E.2d 491 (1960); First National Bank v. Lowery, 17 Ill. App. 2d 288, 149 N.E.2d 660 (1958); American Loan Co. v. See, 298 Ky. 180, 182 S.W.2d 644 (1944); Wisdom v. Keithley,

thief across state lines and assert his title against innocent purchasers on the theory that he who has no title can give no title, so also may the conditional vendor of an automobile removed wrongfully to another state assert his rights successfully in the courts of at least forty-four states.[7] Comity and the practical necessity for uniform law dictates this concurrence. Section 9-103(3) of the Commercial Code then is but a codification of this general proposition.

The enactment of certificate of title statutes, however, created a troublesome fissure in the structure of commercial law. Whereas certificates of title were at one time a tax and police expedient, the states began to require such certificates as muniments of title.[8] While the document was intended primarily as an anti-theft device,[9] its requirement as an indication of all ownership rights was a logical legislative second step. The mobility of the subject matter had rendered inadequate the doubtful notice afforded by the chattel mortgage recordation acts.

Unhappily, the enactment of these laws has been a patchwork affair; the conflict of laws problems have been acute. A number of states have required certificates as conclusive muniments of title.[10] In such a jurisdiction, the importer of a vehicle from a state without such a statute may be allowed to perpetrate a fraud on the foreign owner. Before enactment of the Code,[11] Ohio decided that under a statute making acquisition of title hinge on issuance of a title certificate, the court cannot recognize any ownership interest in an automobile except as such interest is evidenced by a certificate of title issued in accordance with Ohio law.[12] The culprit had removed the vehicle from California to Vermont where no title papers are issued and thence to Ohio. Whatever steps the foreign conditional vendor may have taken at the situs of the contract, and whatever the effect of such precautions there, the clear legislative imperative, said the court, could not be avoided. Similarly, Florida's statute was held to thwart the innocent foreign secured party because the formalities of Florida law had not been observed.[13] But statutes which deliberately fly in the face of comity are rare; the common problem is of more subtle origin.

Eleven states do not have certificate of title laws.[14] When an auto-

237 Mo. App. 76, 167 S.W.2d 450 (1943); West v. Associates Discount Corp., 206 Okla. 44, 240 P.2d 1077 (1952); Lillard v. Yellow Mfg. Accept. Corp., 195 Tenn. 686, 263 S.W.2d 520 (1953); Mosko v. Smith, 63 Wyo. 239, 179 P.2d 781 (1947).

[7] National Bond & Inv. Co. v. Larsh, 262 Ill. App. 360 (1931).

[8] Alabama, Kentucky, Massachusetts, Maine, Minnesota, Mississippi, New Hampshire, New York, Rhode Island, South Carolina, and Vermont do not have certificate of title laws.

[9] The Uniform Motor Vehicle Anti-theft Act was adopted in 1926 by the National Conference of Commissioners on Uniform State Laws. This act provided for notation of encumbrances on the title certificate. The act was withdrawn in 1943 and has been replaced on the recommended list by the Uniform Motor Vehicle Certificate of Title and Anti-theft act.

[10] Florida, Nebraska, Ohio, Pennsylvania, and Texas.

[11] Ohio Laws of 1961, S.B. 5 (effective July 1, 1962).

[12] Kelley Kar Co. v. Finkler, 155 Ohio St. 541, 99 N.E.2d 665 (1951).

[13] Lee v. Bank of Georgia, 159 Fla. 481, 32 So.2d 7 (1947).

[14] Supra note 8.

mobile passes from a certificate state such as Pennsylvania into New York the buyer is apprised of the state of title by the statutory certificate notations, if any. Most states require the surrender of foreign certificates either as a matter of comity, or by statute.[15] Even though succeeding purchasers may have no notice of an infirmity of title, the favorable position of the initial transferee gives New York purchasers a considerable advantage.

When an encumbered vehicle enters a title certificate state from New York, the buyer, as a practical matter, must rely on the integrity of the man with whom he deals.[16] In this respect then, Pennsylvania, through its Code Section 9-103(3), has subjected its citizens to the hazards of interstate trafficking, while at the same time it gives full benefit of antiquated foreign recordation acts to citizens of those states whose failure to enact title certificate laws has created those hazards.

But in at least one important area, the Code operates to improve the position of the domestic buyer. The purchaser from a dealer who himself is the mortgagor enjoys new protection. Section 9-307 provides that whether the security interest is or is not protected at home or abroad,

> a buyer in the ordinary course of business other than a person buying farm products from a person engaged in farming operations takes free of a security interest created by his seller even though the buyer knows of its existence.

Section 1-201(9) defines a buyer in the ordinary course of business as

> . . . a person who in good faith and without knowledge that the sale to him is in violation of the ownership rights or the security interest of the third party buys in the ordinary course from a person in the business of selling goods of that kind but does not include a pawnbroker.

The net effect of these provisions is that a buyer on a used car lot takes subject to encumbrances created by the dealer only if he has actual knowledge that the sale is in violation of that security agreement.[17] In the ordinary course of the automobile business actual knowledge by the purchaser is not very likely if the dealer wishes to conceal the facts. Most statutes that require a transfer of title certificate to pass title, exempt transactions by dealers.[18] Further, title transfer laws may not apply to vehicles coming from out of state. Lastly, it is not uncommon for a dealer to complete the paper work of the transaction for the buyer as a business

[15] Ariz. Rev. Stat. Ann. § 28-303 (1956); Ark. Stat. Ann. § 75-134 (1960); Ga. Code Ann. § 68-408a (Supp. 1961); Ind. Stat. Ann. § 47-2501 (Supp. 1961); Iowa Code Ann. § 321.23 (Supp. 1960); Ky. Rev. Stat. Ann. § 186.020 (1955); La. Rev. Stat. § 32.707 (Supp. 1960); Mich. Comp. Laws § 257.218 (1948); Neb. Rev. Stat. § 60-106 (1952).

[16] See supra note 6.

[17] Section 1-201(25) provides:

> . . . A person "knows" or has "knowledge" of a fact when he has actual knowledge of it.

[18] Ark. Stat. Ann. § 75-150 (1959); Colo. Rev. Stat. Ann. § 13-6-18 (1953); Conn. Gen. Stat. Rev. § 14-166 (1958); Idaho Code Ann. § 49-403 (Supp. 1961); Kans. Gen. Stat. § 81-135 (Supp. 1959); La. Rev. Stat. § 32-705 (Supp. 1960); Mich. Comp. Laws § 257.235 (1948); Wis. Stat. § 342.18 (1957).

courtesy. Hence, the vendee would have no occasion to see a tell-tale foreign certificate, should one exist.

The foreign secured party fares better elsewhere than in a Code state in this situation. In *Bank of Atlanta v. Fretz*,[19] the same trio appear: an innocent foreign mortgagee with an interest perfected in the state of origin, a dealer who has wrongfully removed and wrongfully sold the automobile, and an unsuspecting purchaser. The court held that the mortgagee should prevail since he had taken all reasonable steps. In short, mere possession by the dealer is not enough.[20] The owner must be charged with some oversight or imprudence for the purchaser to prevail. Estoppel can operate only against a party in whom there is some legal fault. Most courts have been willing to cut off the security interest if, in addition to possession by the dealer, other circumstances converge to justify the penalty, such as the leaving of documents, indicia of ownership, in improper hands. The Code makes short work of these distinctions: all interests created by the dealer are cut off by a good faith purchase.[21]

PAUL G. DELANEY

Corporations—Derivative Suits—Security for Expenses under Rule X-10b-5 of the Securities Exchange Commission.—*McClure v. Borne Chemical Co.*[1]—Plaintiffs, stockholders in Borne Chemical Co., brought a

[19] 148 Tex. 551, 226 S.W.2d 843 (1950). The case is cited with approval by the court in the principal case, but with no comment upon the fact that resale was by a dealer.

[20] The mortgagee who has left encumbered goods with the mortgagor engaged in the sale of such goods may well be deprived of his rights as against an innocent purchaser on theories of agency, waiver, or estoppel. But the law chose not to make this an absolute proposition. Possession alone is inconclusive. "The law takes into account not simply the deception of the subsequent buyer by the appearance of title in the possessor of the goods, but also whether this appearance of title was created by the original owner for a purpose so essential and proper that the original title must be protected irrespective of the injury to the subsequent buyer." 2 Williston, Sales § 312 (rev. ed. 1948).

Mori v. Chicago National Bank, 3 Ill. App.2d 49, 120 N.E.2d 567 (1954); Rand's Discount Co. v. Universal C.I.T. Corp., 10 App. Div.2d 240, 198 N.Y.S.2d 341 (1960). The classic case of the watch left for repairs with a jeweler typifies this principle. Zendman v. Harry Winston, Inc., 305 N.Y. 180, 111 N.E.2d 871 (1953). The rule is no less applicable to automobile cases. Budget Plan Inc. v. Savoy, 336 Mass. 322, 145 N.E.2d 710 (1957).

See also the Uniform Sales Act, 1 U.L.A. § 23(1); Uniform Conditional Sales Act, 2 U.L.A. § 9 (Supp. 1960); Uniform Trust Receipts Act, 9A U.L.A. § 9 (1951). These laws all manifest particular concern for the innocent purchaser. Yet all accept the premise that mere possession by the dealer is not enough. On the other hand, case law has been said to have eroded the common law principle through a particular finding of negligence by the mortgagee. First National Bank v. Hermann, 275 App. Div. 415, 90 N.Y.S.2d 249 (1949).

[21] In a somewhat similar situation the Code again completely abrogates the old principle. Section 2-403(2) states: "Any entrusting of possession of goods to a merchant who deals in goods of that kind gives him power to transfer all rights of the entruster to a buyer in the ordinary course of business."

The voidable title doctrine, as codified in § 2-403(1), has not yet been extended to conditional sales. See, generally, 49 Ky. L.J. 437 (1961).

[1] 292 F.2d 824 (3d Cir. 1961).